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GAO

United States
General Accounting Office
Washington, D.C. 20548

Health, Education, and
Human Services Division

B-265684

June 10, 1996

The Honorable Thomas J. Bliley, Jr.
Chairman, Committee on Commerce
House of Representatives

Dear Mr. Chairman:

Medicaid is the largest federal program providing financial assistance to state governments. States received over $80 billion in fiscal year 1995, and the Congressional Budget Office estimates that they will receive $898.4 billion in federal funds between fiscal year 1996 and fiscal year 2002. The Congress is now considering alternatives that would slow the growth in federal Medicaid spending by giving states more flexibility in the administration of the program and by changing the mechanism for allocating federal assistance among states.

This letter responds to your request for an explanation of the relationship between federal funding and state funding needs under the current open-ended entitlement program and how it would change under H.R. 3507, being considered by your Committee. Under the open-ended entitlement the level of assistance provided to the poor varies from state to state depending on how many people are made eligible under state law and how extensive are the services the state provides. In contrast, under H.R. 3507 the distribution of federal assistance to states would be much less related to state spending patterns and become more closely related to measures of state funding needs, such as the number of poor, elderly, and disabled.

FEDERAL FUNDING NOT BASED ON STATE FUNDING NEEDS

The amount of federal aid that a state receives under Medicaid is not closely linked to measures of its potential funding needs. In many instances, states with larger numbers of poor and disabled individuals receive less federal assistance than states with both larger numbers of those in need and weaker tax bases. New York, for example, has fewer poor people than California yet it received $12.5 billion in federal assistance in fiscal year 1995 while California, with more people in need, received less than $9.2 billion that year. When expressed in terms of funding per person in poverty, New York received 60 percent more than California; more than $4,350 per person compared with less than $1,725 per person in California.

Because the federal government matches whatever states spend on eligible services, states with the most generous eligibility requirements, that offer more extensive services, and that provide higher provider reimbursement rates receive more federal funding. Consequently, states with greater numbers of needy individuals can receive less federal aid because of their more restrictive eligibility rules and because they provide fewer services.

MOST FEDERAL PROGRAMS PROVIDE FUNDING BASED ON STATE NEEDS

The current linkage between state needs and the amount of federal assistance a state receives under Medicaid does not reflect how most federal grant programs are designed. Aside from the major entitlement programs (Medicaid, Aid to Families With Dependent Children, and Foster Care), most other federal grant programs distribute federal assistance on the basis of need measures (for example, high risk population groups such as the poor, children, or the elderly) rather than on the basis of state spending patterns.

A recent example of needs-based targeting is the Ryan White Comprehensive AIDS Resources Emergency (CARE) Act reauthorized by Congress earlier this year. The Senate Labor and Human Resources Committee and your Committee revised the formula used to distribute CARE Act funds to states and metropolitan areas to improve the needs-based targeting of that program. The new system would strengthen the relationship between federal funding and people in need by more closely linking the amount of federal aid a state or metropolitan area receives with the number of people with acquired immunodeficiency syndrome (AIDS).

Other examples of need-based targeting include the Chapter 1 program for the Educationally Disadvantaged and the Maternal and Child Health program, which target federal funding based on the number of children in poverty. Similarly, the Airport Improvement program provides funding based on the number of passengers using an airport and the Older Americans Act allocates federal funding based on the number of elderly. Based on work currently underway, it appears that over 90 percent of federal formula grant programs target funding based on measures of state need.

THE MEDICAID RESTRUCTURING PLAN WOULD GRADUALLY SHIFT FEDERAL FUNDING TO A NEEDS-BASED SYSTEM

A restructured Medicaid program under provisions in H.R. 3507 would gradually realign federal funding over a number of years so that it will be more closely related to state needs rather than state spending patterns. This would be accomplished by linking federal allocations to the number of people in poverty and giving greater weight to the number of elderly and disabled for whom care is more expensive. Additional adjustments would be made to account for cross-state

differences in the cost of health care, and low-income states' matching rates would continue to be higher.

Shifting to a needs-based funding system will be accomplished by allowing funding for states like California, whose federal funding is low in relation to the number of people in need, to grow at above average rates. Conversely, funding for states like New York would grow at slower rates until funding for all states is brought into line with state needs.

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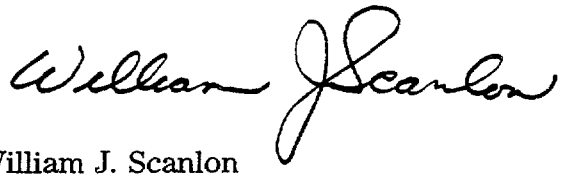
If you have any questions regarding this letter or if we can be of further assistance, please call Jerry Fastrup, Assistant Director, at (202) 512-7211 or me at (202) 512-4561.

Sincerely yours,



William J. Scanlon
Director, Health Systems Issues

(118137)

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General Accounting Office
Washington, D.C. 20548

Health, Education, and
Human Services Division

B-272252

June 10, 1996

The Honorable Michael Bilirakis
House of Representatives

Dear Mr. Bilirakis:

This letter responds to your request for comments on an analysis entitled, "Florida's Fair Share." That analysis questions the appropriateness of the Medicaid funding formula now contained in H.R. 3507, noting that Florida's projected allocations for fiscal years 1996 through 2002 are less than those projected for Pennsylvania and Ohio, even though Florida has more people and a larger proportion of elderly individuals than either state.[1]

Our review of the formula in H.R. 3507 indicates that in each year the new formula would cause the distribution of federal Medicaid funding to become progressively more closely aligned with states' poverty populations and to reflect the proportions of the populations who are elderly.

Under current law, federal funding of state Medicaid programs is not based on the size of state populations. Rather, the program is an open-ended matching program that provides more generous matching rates for low-income states. Consequently, the more a state spends on benefits for eligible recipients and the lower its per capita income, the more it receives in federal dollars. For example, Florida spends less than Pennsylvania and receives less in matching federal funds (see table 1). In contrast, Ohio spends less yet receives more in federal matching because its lower per capita income results in a higher federal matching percentage (61 percent compared with Florida's 56 percent).

[1]The analysis also points out that on a proportionate basis, North Carolina also receives more. That is, Florida has twice the population of North Carolina but would not receive twice the funding under the proposal.

Table 1: State Medicaid Spending and Matching Federal Funds for Fiscal Year 1995

Millions of Dollars

State	State spending	Federal matching percentages	Federal matching funds
Florida	$2.6	56	$3.4
Pennsylvania	3.4	54	4.0
Ohio	2.4	61	3.8
North Carolina	1.4	64	2.5

The formula described in H.R. 3507 would change this by establishing a target for federal funding in proportion to the number of poor in each state. The target is also adjusted for the proportion of Medicaid beneficiaries who are elderly or disabled to reflect their higher cost of care compared with children and non-elderly adults. Each state's federal allocation is allowed to increase depending on the differences between current federal funding and the target. This will allow federal funding to grow more rapidly in states like Florida where funding is low compared with the size of the population. Similarly, in states like Pennsylvania and Ohio, where funding is comparatively high, federal funding would grow at slower rates. Eventually, each state's share of funding more would more closely reflect its number of poor as the effect of differing growth rates becomes more influential.

Table 2 shows what each state's share of federal funding was in fiscal year 1995 and how the differences in growth rates will affect the share of federal funding in fiscal year 2002.

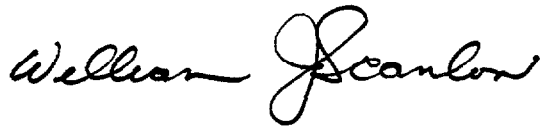
Table 2: State Shares of Federal Funding

State	Funding share (FY 1995)	Average annual growth rate (1996-2002)	Funding share (FY 2002)
Florida	3.9%	7.5%	4.4%
Pennsylvania	4.6	4.8	4.5
Ohio	4.3	5.1	4.2
North Carolina	2.8	5.1	2.7

Thus, by giving states like Florida higher growth rates, the formula described in H.R. 3507 will enable them to receive federal funding in future years in proportion to the poverty population as the cumulative effects of higher growth rates take on increasing importance. Florida is not receiving federal funding in proportion to its poverty population under current law because Florida chooses to spend less for Medicaid than either Pennsylvania or Ohio. As a result, Florida receives less in federal matching funds.

If you have any questions regarding this letter or if we can be of further assistance, please call Jerry Fastrup, Assistant Director, at (202) 512-7211 or me at (202) 512-4561.

Sincerely yours,



William J. Scanlon
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